



Ref:

18 September 2002

FILE No:
DOC:
MARS/PRISM:

General Manager  
Regulatory Affairs - Electricity  
Australian Competition and Consumer Commission  
PO Box 1199  
DICKSON ACT 2602

Dear Michael

**APPLICATIONS FOR AUTHORISATION No. A90797, A90798, A90799) –  
CHANGES TO NATIONAL ELECTRICITY CODE REBIDDING RULES**

Tarong Energy is pleased to make this submission in response to the Commissions Draft Determination dated 3 July 2002 and the Pre-Determination Conference held on 13 August 2002.

**The NECA Process**

***Who May Propose Code Changes***

The National Electricity Code provides that a Code Participant or any other person may make a proposal for changing the Code. This must be done in writing to NECA and must include a brief statement of the reasons why a change is necessary or desirable. It is clear that the ability to propose changes to the Code is not intended to be restricted to just Code Participants, or even to those persons such as industry or consumer groups, who may be described as interested persons.

Given that there are essentially no restrictions on who may propose a change to the Code, it is difficult to envisage circumstances when NECA, the Code Administrator, would feel it necessary to initiate its own proposal for change. Any person whether a Participant or not, who believes the Code is deficient in some manner has a right to approach NECA with a proposal for changing the Code.

Tarong Energy is concerned that NECA has taken it upon itself to propose these changes to the Code, when any person could have initiated the process. The concern is that NECA has voluntarily adopted this role of proponent when both NECA, and its Chief Executive Officer, have mandatory roles in assessing and progressing proposed changes to the Code.

It is acknowledged that the Code provides that NECA may itself propose a Code change, however Tarong Energy believes that, as a matter of prudent policy, NECA should not take on this discretionary role in any but the most exceptional circumstances.

P:\MTRAD\Regulation\Rebidding Submission to ACCC.doc

Tarong Energy is a registered business name of Tarong Energy Corporation Limited ABN 52 078 848 736

Handwritten notes in a box, including the word "copy" and some illegible scribbles.

**TARONG ENERGY  
CORPORATION LIMITED**  
ABN 52 078 848 736  
  
LEVEL 10 AMP PLACE  
10 EAGLE ST BRISBANE  
GPO BOX 800  
BRISBANE Q 4001  
TELEPHONE +61 7 3228 4333  
FACSIMILE +61 7 3228 4300  
  
TARONG POWER STATION  
PO BOX 15  
NANANGO Q 4615  
TELEPHONE +61 7 4160 9444  
FACSIMILE +61 7 4160 9305  
  
WIVENHOE POWER STATION  
PO BOX 38  
FERNVALE Q 4306  
TELEPHONE +61 7 5426 7455  
FACSIMILE +61 7 5426 7453

### ***The Dual Roles of the Chief Executive Officer of NECA***

A key reason why Tarong Energy considers NECA should exercise great reluctance in proposing changes to the Code is that the Code requires the Chief Executive Officer of NECA to chair the Code Change Panel. If NECA is the proponent of a Code change proposal this immediately places the chair of the Code Change Panel in a conflict of interest.

For NECA to propose a Code change would require a decision by the Board of Directors of NECA. How is the Chief Executive Officer of NECA, in the role as chair of the Code Change Panel, expected to assess a proposal put forward by his own Board of Directors? The Code and the legislation provide no guidance for this situation.

### **The NECA Application**

#### ***Evidence of a Problem***

At no stage in the process of proposing these changes to the Code has NECA ever been able to clearly and objectively identify the problem that the changes are seeking to address. The "problem" as far as Tarong Energy has been able to identify is that some commentators have been concerned to see sometimes significant fluctuations in five minute spot market prices. With essentially no analysis these commentators have then jumped to a conclusion that this spot market volatility is evidence of generator market power and that the rules should be modified to prevent it. Moreover, there is a presumption that five minute spot market volatility feeds directly into longer term contract pricing.

There has been no proper analysis to determine that spot market volatility, as opposed to longer run price outcomes, drives the wholesale energy price component of the delivered cost of electricity to customers.

Even if NECA had adduced evidence to suggest there is a problem in the functioning of the market, they have made no attempt to establish that the proposed changes will address that problem. NECA have never explained how the practical operation of any of their proposals would ameliorate any specific incident in the past that has prompted the changes.

Even if there is a structural problem in the NEM with the presence, exercise and abuse of market power, which has not been objectively demonstrated, NECA has failed to consider whether alternatives to changing the rebidding rules would deliver a better outcome. Structural solutions such as significantly increasing the level of interconnections between regions and firmer inter-regional trading instruments would tend to increase the size of the market away from regional pools to a truly national market. Supposed problems of market power within smaller regions would then be addressed by effectively making them part of larger regions, which are better able to support a larger number of competitors.

In seeking to address the symptoms of a supposed problem, NECA and the Code Change Panel have failed to conduct an appropriate root cause analysis. This deficiency in analysis could be addressed by appropriately rigorous regulatory analysis as discussed below.

### ***Best Practice Regulatory Design***

As the body with primary responsibility for the key regulatory document in the market, NECA should seek to adopt best practice in regulatory management activities. Tarong Energy has previously advocated that NECA and Code Change Panel should accompany each Code change proposal with a statement of regulatory impact, or equivalent. Such a report will address the following elements:

- the policy objectives of the proposed change and the reasons for them,
- the way the policy objectives will be achieved by the proposed change and why this way of achieving them is reasonable and appropriate,
- an explanation of how the proposed change is consistent with the policy objectives of the authorising law,
- if the change is inconsistent with the policy objectives of other legislation (eg the *National Competition Law*, the *Trade Practices Act*, the *Legislative Standards Act*, the *Judicial Review Act*), an explanation of the relationship with that legislation and the reasons for the inconsistency,
- identify any reasonable alternative way(s) of achieving the policy objectives (including the option of not making any change) and why such alternatives have been rejected,
- an assessment and quantification of the impacts, benefits and costs of implementing the proposed change and a comparison of the impacts, benefits and costs of all reasonable alternatives, and
- an assessment of the consistency of the proposed change with "fundamental legislative principles" and, if inconsistent with "fundamental legislative principles", the reasons for the inconsistency.

These elements are taken from the *Statutory Instruments Act 1992 (Qld)* but could be readily adapted to suit the circumstances of the Code Change Panel. Tarong Energy is of the view that such a statement of regulatory impact would also greatly assist the Commission in assessing applications for authorisation.

### **The Commissions Draft Determination**

#### ***The Criteria for Authorisation***

In considering an application for authorisation to change provisions of the Code, the Commission is required to adopt a public benefit criteria. Specifically the Commission may only grant the authorisation if it is satisfied that there is a public benefit and if that benefit would outweigh any anti-competitive detriment suffered by authorising the changes.

It does not appear open to the Commission to grant authorisation in any other circumstances.

### ***Examining Price Spikes***

In assessing the proposed Code changes the Commission engaged several consultants to assist the Commission in examining market data. The brief provided to the consultants required them to limit their analysis to only those occasions when spot market prices spiked. Such a selective sampling policy must lead to skewed results and any conclusions reached from such analysis are open to question.

Tarong Energy is of the view that any conclusions reached from such a selective sampling policy will be insufficient so satisfy the public benefit test set out in the Trade Practices Act.

### ***The Good Faith Requirement***

In its Draft Determination the Commission has authorised changes to the Code to require that bids and rebids made by Market Participants be made in good faith. Tarong Energy is concerned that good faith, as a legal concept, is applied where a person is in a relationship of trust vis a vis a second person. Thus company directors must act in good faith in directing the affairs of a company.

NECA has suggested that good faith in this context means nothing more than reflecting your genuine intentions at the time the bid or rebid is made. If that is what was intended then that is what the Code Change Panel should have recommended originally. Instead of good faith, perhaps a better concept would be for bids and rebids to represent a bona fide intention to trade at the prices and quantities stated.

At the very least Tarong Energy believes the Commission should require that good faith be properly defined, to avoid unnecessary regulatory risk being imposed on trading participants.

### ***The Use of "Suggestions"***

Tarong Energy is very concerned that the Commission has put forward a range of suggested further Code changes that it believes will deliver beneficial outcomes. In making these suggestions the Commission appears to have exceeded the authority granted to it by the Trade Practices Act. Tarong Energy also believes the Commission has made the same error as NECA in not conducting proper analysis to demonstrate the beneficial outcomes it asserts will result from the suggestions.

### ***The NECA Way Forward***

At the Commissions Pre-Determination Conference called by the South Australian Jurisdiction and Macquarie Generation and held on 13 August 2002, NECA presented some revised thinking on this subject. This was subsequently followed up with a letter to all market generators setting out specific proposed changes to the wording of the Code to give effect to the revised thinking. These alternate Code changes were also communicated to the Commission with the invitation to consider these as part of the current determination process.

**Enhancements or Changes?**

The Commission will only be empowered to authorise these latest NECA proposals that are in respect of the original application for authorisation (per s. 90(1)(a) of the Trade Practices Act). Tarong Energy acknowledges that those elements of the NECA revisions that seek to give effect to the conditions specified by the Commission in the Draft Determination should probably be seen as being in respect of the original application.

However a number of elements of the latest NECA proposals seek to give effect to the suggestions made by the Commission in the Draft Determination. Tarong Energy is of the view that these proposals are so substantially different from the original application that any authorisation of them could not be considered to have been in respect of the original application.

**Conclusions**

Tarong Energy remains concerned with the processes for proposing changes to the Code that place the chief executive officer of NECA in a position of conflict of interest between the roles of Chairman of the Code Change Panel, and an officer of NECA. The conflict arises because the NECA Board refers matters to the Code Change Panel, and then determines which Code change proposals are forwarded to the Commission for authorisation.

At no stage have NECA or the Code Change Panel clearly articulated a problem with the NEM that would be amenable to a solution based on changes to the Code. Tarong Energy is also dissatisfied with the analysis of the NECA proposals conducted by the Commission and believes it is not sufficient to support a conclusion that a net public benefit has been identified. Tarong Energy is also concerned that the Commission's use of suggestions in the Draft Determination goes beyond the powers granted to the Commission by the Trade Practices Act.

Finally Tarong Energy does not believe the Commission is entitled to authorise the revised NECA proposals that purport to give effect to the Commission's suggestions. In saying that Tarong Energy concedes it is probably open to the Commission to authorise those elements that give effect to the conditions of authorisation set out by the Commission in the Draft Determination.

Yours sincerely



Greg Hesse  
SENIOR MANAGER, REGULATORY AFFAIRS

Enquiries:

Telephone (07) 3228 4352  
Facsimile (07) 3228 4319